MONETIZATION FIELD MANUAL

P.L. 480 Title II Programs

Office of Food for Peace

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ACRONYMS AND GLOSSARY

AER	Annual Estimate of Requirements. A table submitted with a DAP or PAA which is signed by the cooperating sponsor and estimates the quantities of commodities that will be required for the coming year.
BHR/FFP/POD	Bureau for Humanitarian Response/Office of Food for Peace/ Program Operations Division at the U.S. Agency for International Development.
Bank Guarantee	A document issued by a bank by which the bank agrees, on behalf of the buyer, to ensure that all obligations set forth under a contract, including payment in full, will be met by the buyer, provided the seller demonstrates full discharge of his obligations through presentation of specified documents within a predetermined time frame.
Bellmon Amendment/ Determination	An analysis in the proposal submitted to the Mission Director by the Cooperating Sponsor, pursuant to section 403(a) of P.L. 480, showing that a commodity is suitable for monetization (or distribution) in that country, adequate storage is available in the recipient country, and import of the commodity will not result in a substantial disincentive to or interfere with domestic production or commercial marketing of the commodity in that country. The Mission makes the determination on the adequacy of the analysis, subject to final approval of all aspects of the proposal by FFP.
C&F	Commodity and Freight. A price quotation that includes the cost of merchandise and freight charges to a specific destination.
CCC	Commodity Credit Corporation. A corporate agency and instrumentality of the United States within the U.S. Department of Agriculture.
CS	Cooperating Sponsor. An entity, within or without the United States, governmental or not, such as the foreign government, the American Red Cross, the intergovernmental organization, or the private voluntary organization or cooperative, which enters into an agreement with the U.S. Government for the use of agricultural commodities or funds.
Call Forward	A request initiated by the field office of a CS for the delivery of a quantity of food commodities to a particular country program for use over a specified period of time.
Commodity(ies)	Food or feed transferred or available for transfer to cooperating sponsors.
Commodity Specifications	The required attributes of the commodity being requested.
Cost Recovery	The concept that the expenses incurred by the U.S. Government in procuring and transporting a P.L. 480 Title II commodity are offset by the revenue realized when the commodity is monetized.
DAP/PAA Guidelines	A document, updated periodically by BHR/FFP, that provides guidance to Cooperating Sponsors on the preparation of Development Activity Proposals and Previously Approved Activity reports, two new designations for "Operational Plan" as defined in Regulation 11.

ACRONYMS AND GLOSSARY (cont'd.)

Discharge Survey	A report that is prepared at the time a commodity is discharged from the vessel of transport at the destination port and documents the condition of the cargo.
FAS	Free Alongside Ship. Includes all costs of transportation and delivery of the goods to the dock.
FEWS	Famine Early Warning System, funded by USAID. Tracks vulnerability to famine in food insecure countries.
FFP/D	The Director of the Office of Food for Peace.
Food for Peace	The general term applied to the food donation program authorized by the Agricultural Trade Development and Assistance Act of 1954 (P.L. 480), as amended.
GIEWS	Global Information and Early Warning System, created under the Food and Agricultural Organization in Rome. Estimates food production and food needs in famine-prone countries.
Hard Currency	A currency widely used as a means of exchange in international transactions.
Indicators	Measurements used in determining the degree of progress that has been made toward achieving an objective.
Letter of Credit	A commercial instrument issued by the importer's bank to the exporter that establishes a documentary basis for the exporter getting paid, provided the exporter complies with the exact terms of the credit.
LIFDC	Low Income, Food-Deficit Countries include all food-deficit (ie. net importing basic foodstuffs) countries with per capita GNP not exceeding the level used by the World Bank to determine eligibility for International Development Association (IDA) (soft loan) assistance.
Mission	For purposes of this document, the representative office of USAID in a country outside the United States.
MT	Metric Tonnage.
Monetization	The selling of agricultural commodities to obtain foreign currency for use in U.S. assistance programs.
Oligopoly	A market dominated by only a few parties.
PAA	Previously Approved Activity. The report submitted annually by a CS that requests a fiscal year allocation of commodities and dollars for an ongoing Title II activity.

ACRONYMS AND GLOSSARY (cont'd.)

P.L. 480 Title II	An "Emergency and Private Assistance" program to provide agricultural commodities to foreign countries on behalf of the people of the United States to: address famine or other urgent or extraordinary relief requirements; combat malnutrition, especially in children and mothers; carry out activities that attempt to alleviate the causes of hunger, mortality or morbidity; promote economic and community development; promote sound environmental practices; and carry out feeding programs.
Parastatal	A business with some degree of autonomy that is otherwise owned and controlled by a government.
Pipeline	Commodities or funds unused during a financial year or reporting period that are transferred to the budget or planning levels for the following financial or reporting year. Also sometimes referred to as "carryover." A "pipeline analysis" is a report of the "carried forward" commodities or funds.
Results Report (R2)	Cooperating Sponsor reporting document summarizing progress made during the year's activities.
Third-Country Monetization	A monetization where commodities are sold in one country and the foreign currency generated is used in that country and/or another country in the same region.
Title III (P.L. 480)	A "Food for Development" program under which agricultural commodities are donated typically on a government to government basis to least developed countries.
UMR	Usual Marketing Requirements. Analysis required under P.L. 480 to ensure that P.L. 480 sales programs do not disrupt world commodity prices or normal commercial trade patterns betwen the importing country and other friendly countries.
USAID/W	United States Agency for International Development in Washington, D.C.
USDA	United States Department of Agriculture
Umbrella Monetization	Two or more Cooperating Sponsors operating in a specified country or region monetize their commodities jointly for purposes of: containing costs related to marketing and market analysis; avoiding duplication of effort; increasing the volume of commodities to be monetized which enhances competitiveness; and achieving greater supply impacts.
WFP	WFP means the World Food Program, which enters into an agreement with the U.S. Government for the use of agricultural commodities and which is directly responsible under the agreement for administration and implementation of programs involving the use of commodities made available to meet the requirements of eligible recipients.

INTRODUCTION

I. PURPOSE

This Monetization Field Manual outlines policy and operational procedures for private voluntary organizations (PVOs) and cooperatives, acting as Title II Cooperating Sponsors, in the design, implementation, management and evaluation of P.L. 480 Title II partial and full monetization transactions in emergency and non-emergency contexts. The roles and responsibilities of Title II Cooperating Sponsors, USAID Missions, and USAID/W, including FFP/D, are also clarified.

II. AUTHORITY

This manual is supplemental to the Agricultural Trade Development and Assistance Act of 1954 (P.L. 480), as amended, and USAID Regulation 11 (22 CFR Part 211) dated May 7, 1992. This Monetization Field Manual supersedes the manual dated August, 1988. In the event of any inconsistency, Regulation 11 takes precedence over the manual.

III. RELATED DOCUMENTS

The following references, which further articulate USAID monetization policy and operational procedures, should be used in conjunction with these guidelines:

- USAID Regulation 11 dated May 7, 1992;
- Automated Directive Systems (ADS) with supplemental reference Handbook 9;
- USAID "Background Paper and Guide to Addressing Bellmon Amendment Concerns on Potential Food Aid Disincentives and Storage," dated July 1985;
- State Cable 086836 - Bellmon Certification Requirements for P.L. 480 Title II Activities, dated May 14, 1998;
- OMB Circular A-122;
- Annual USAID DAP/PAA guidance for the preparation of Title II development proposals and reporting documentation;
- Title II Monetization Evaluation Report dated, March 29, 1996;
- Title II Close-out Plan Guidance, dated September, 1996;
- PVO Guidelines for Title II Emergency Food Proposals and Reporting (Draft), dated January 26, 1998.

TITLE II MONETIZATION

POLICY FRAMEWORK

I. BACKGROUND

Since the beginning of Title II monetization in 1986, the use of monetization proceeds has grown dramatically to become a critical resource for Cooperating Sponsors (CSs). The 1996 reauthorization of P.L. 480 increases to 15 percent the minimum percentage of the aggregate value of non-emergency Title II commodities to be made available annually for monetization by PVOs and cooperatives. In addition, the use of third-country monetizations, where commodities are sold in one country and the foreign currency generated is used in another country in the same region, is now permitted in both emergency and development programs.

A 1995 U.S. Department of Agriculture (USDA) study entitled *Food Aid Needs and Availabilities - Projections for 2005* states that "food aid needs will nearly double over the next decade, even with reasonably optimistic assumptions about recipient countries' ability to produce their own food or have the financial capacity to import food commercially." Coupled with growing needs for food aid, especially in sub-Saharan Africa and South Asia, is the reduction in real terms of USAID's development budget--both food and non-food resources. Scarcity of U.S. Government surplus food stocks, requiring that virtually all food aid be purchased in commercial U.S. markets, also contributes to the current context of rising demand and declining supply. Other challenges involve the increased pressure on USAID and CSs to demonstrate concrete progress toward food security goals and the continuing debate over whether the distribution or the monetization of commodities is the most efficient and effective use of the food aid resource.

In February of 1995, USAID issued its *Food Aid and Food Security Policy* paper, which promotes the integration of food aid with other USAID assistance resources and the use of monetization proceeds to complement activities aimed at enhancing agricultural productivity and improving household nutrition. The policy also emphasizes the need to strengthen performance monitoring and evaluation systems to demonstrate more quantitatively and qualitatively the food security impact of food aid programs. The purpose of this manual is to clearly define a new set of policy guidelines and operational procedures to ensure that Title II monetization directly contributes to the food security objectives defined in the Agency's *Food Aid and Food Security Policy* paper and to improve the management of monetization activities and resources.

II. PROGRAMMING PROCEEDS TO ACHIEVE FOOD SECURITY OBJECTIVES

USAID's *Food Aid and Food Security Policy* paper is the foundation of any review of Title II activities, including those supported by Title II foreign currency. Priority will be given to proposals in which the use of the foreign currency generated has the greatest potential for achieving food security results for vulnerable people. Specifically, it is USAID’s policy that foreign currency generated from monetization must be programmed to support the objectives of increased agricultural productivity and improved household nutrition.

If a USAID Mission wishes to exercise program direction or management control, or both, over a given activity, then the appropriate implementation mechanism is a contract and not a grant and donation. (See USAID's Automated Directives System Section 304.5.) P.L. 480 is a grant and donation program, and if the Mission wishes to directly program monetized food aid or to use monetized food aid in support of host government-sponsored programs, then the appropriate implementation mechanism is Title III, not monetized Title II. As with all other grants, both food and non-food, provided by USAID, Title II grants and donations are provided to support the program activity identified, designed and managed by the grantee or a Title II CS.

III. MONETIZATION AND FOOD SECURITY OBJECTIVES

Title II food aid monetization is typically built around two objectives. First, Title II food aid monetization is programmed to enhance food security. Second, Title II food aid is used by a CS to generate foreign currency to support development activities.

Monetization offers the potential to improve the marketing of food to permit greater access to those who are food insecure. Indeed, there is an important direct link between food security and how food aid is monetized. The process of monetizing can be used to promote low-cost, competitive food markets by encouraging investment in transportation, infrastructure and human capital (traders, entrepreneurs). In essence, food aid monetization can enhance long-term food security by encouraging the development of competitive food marketing systems that have built-in incentives to provide the poor with affordable staple foods.

Thus, Title II monetization must address three objectives:

1. to generate the maximum feasible amount of foreign currency funds for Title II food security activities;

2. to enhance household access to food, at least in the short run; and

3. to encourage, where appropriate, the development of competitive food marketing systems.

These objectives rest upon the underlying precept that, above all, food aid monetization efforts must strive to "do no harm" to producers' incentives, fragile local food markets, and low-income consumers. They also stem from the belief that food aid is a unique resource that does have enormous potential to contribute to long-term sustainable development. Above and beyond the generation of funds for food security activities, monetization is one more tool among the set of programming options available to enhance the food security of vulnerable households through the use of U.S. food commodities.

IV. AVOIDING DISINCENTIVE EFFECTS OF MONETIZED FOOD AID

Food aid practitioners have long recognized the potential for food aid, whether through direct distribution or monetization, to create disincentives for domestic food production. This recognition, however, does not always translate into food aid programming that "does no harm." Legislation and regulations require that, before P.L. 480 food aid can be provided for direct distribution or monetization, a CS must prepare a Bellmon Amendment determination in accordance with Section 403(a) of P.L. 480, to establish that: a) adequate storage facilities are available in the recipient country, and b) "the distribution of the commodities in the recipient country will not result in a substantial disincentive to or interference with domestic production or marketing in that country." Too often Bellmon analyses and determinations reflect serious shortcomings in demonstrating a clear understanding of the market in which a monetization is to take place. They also frequently do not cover the requirement of Section 403(b) of P.L 480, that the Administrator "shall ensure that the importation of United States agricultural commodities and the use of foreign currency for development purposes will not have a disruptive impact on the farmers or the local economy of the recipient country." Current policy requires that if a Mission is present in the country where commodities are being monetized, the Mission must make a determination from the CS's Bellmon analysis that the statutory requirements are met.

When food is appropriately targeted and distributed to those without adequate cash income to purchase in the market, disincentive effects are often, although not always, minimized. For example, feeding programs often target poor consumers that have calorie deficits due to an inability to secure food either through production or through the market. In such cases, direct distribution of food aid can be a net addition to total food availability with minimal effect on agricultural production incentives and domestic food prices.

Monetized food aid, however, does not have these advantages because in most cases it is eventually purchased by consumers through normal marketing channels. As a result, it can have serious negative and positive impacts on food prices, marketing, and production incentives. In addition, since any food system is composed of numerous participants (farmers, traders, processors, retailers and consumers), the impact upon different participants can vary greatly. More affordable retail food prices can benefit urban consumers but translate to lower produce prices for farmers. Similarly, sales of food aid in the "hungry season" right before harvest may stabilize prices and benefit consumers. However, such sales may also destroy incentives for food traders to engage in intra-seasonal storage and to create local capacity to deal with seasonal food insecurity. The timing of a monetization, not just the volume of commodity, must be considered in the overall context of food flows.

The effects of monetizing must be carefully scrutinized. The key issue is not so much whether monetization will have an effect on the market but rather the magnitude of the effect. Is it tolerable or desirable? Is it "substantial?" More attention must be devoted by the CS and USAID Mission to understanding and minimizing potential disincentives while maximizing the potentially positive effects of monetized food aid. In response to increased attention to preparing thorough Bellmon analyses, the key elements that must be considered during the preparation of a Bellmon determination are outlined in Appendix A.

V. NEED FOR MARKET ANALYSIS

Because the rationale for monetizing, or the decision not to monetize, flows primarily from market factors, the analysis of food market structure, conduct, and performance must be a central component of all food aid monetization efforts. For this reason, the Title II CS and USAID Mission must increasingly demonstrate throughout proposal submissions, activity implementation, and results reporting a clear understanding of the markets in which they operate. Approval of proposals utilizing funding from monetizations will be contingent upon demonstration of an understanding of the likely effects of the monetization on the local market.

There are several well-developed frameworks that can be used to analyze food markets. One of the most common, developed by economists and refined by business school practitioners, involves recognizing the links between the structure of a market (the number of buyers and sellers, the nature of the commodity, etc.), the conduct of participants (how prices are set, what rules are followed, etc.) and the eventual performance of the market. Performance is simply judged by the degree to which the market meets a diverse set of goals; some of the goals of a food marketing system might be technical efficiency or affordable retail food prices.

Although market analysis is often thought of as a highly quantitative exercise, much can be gained from a descriptive analysis of the structure, conduct and performance of a food market. Such analysis can be well suited to low-cost rapid appraisal techniques. At its most basic, food market analysis boils down to viewing the food system as a step-by-step series of inter-linked transactions and transformations. An understanding of "how the system works" can be gained by an initial inventory of all participants, followed by open-ended conversations and interviews with participants. In response to this increased emphasis on understanding markets, suggested procedures for conducting a market analysis are provided in Appendix B.

USAID recognizes that this increased attention to market analysis requires that USAID increase its own technical capacity or refocus existing technical capacity so that a determination can be made as to whether a CS submitting a proposal has demonstrated an understanding of the local market and how its monetization will affect that market. Moreover, USAID recognizes that, although it is the CS's responsibility to conduct a Bellmon analysis (unless one already exists for the current fiscal year and the relevant commodity and Metric Tonnage (MT) level), the CS should not carry the burden of expanded market analysis alone. USAID, primarily through its field Missions but also through its technical offices, is committed to providing technical assistance to the CS to enhance its capacity to analyze markets and, ultimately, to design and execute market-friendly monetizations. This is an integral part of the statutory requirement that the appropriate United States field mission concur in the CS proposal before it is submitted to USAID/W. At the same time, USAID strongly encourages the CS executing a monetization to continue its efforts in developing marketing expertise. Similarly, it is the Mission Director or principal officer in-country who must make the Bellmon Determination, as under Delegation of Authority 902, no Title II activity may take place in a country without clearance of the principal USAID officer, who then will be responsible for monitoring all food aid activities in the country. The CS is encouraged to tap existing Section 202(e), Institutional Support Assistance (ISA), foreign currency or other resources for the purpose of increasing technical capacity to carry out successful monetizations that, at a minimum, "do no harm." Potential collaboration with national and international institutions with the technical expertise to conduct market analyses should also be considered.

VI. OPEN AND COMPETITIVE SALES

A decade ago, many developing countries had tightly controlled marketing systems, and negotiated pricing arrangements may have been the only option for the CS choosing to monetize. Today, however, most developing countries have made substantial food policy reforms and now permit a wide range of private sector marketing activities. Nonetheless, too often the CS monetizes food aid by selling directly to monopolistic parastatals and oligopolistic traders and processing firms even when small-scale private buyers exist. The reason for this is relatively easy to understand: negotiated sales to one buyer or several large buyers eliminates the complexity and higher costs associated with conducting auctions or making sales in small lots to numerous buyers.

By neglecting small-scale buyers and overlooking the potential for alternative marketing channels to meet consumer food needs, sales to parastatals and oligopolies adversely affect the very people food aid is meant to help. The net effect is often to exclude statutorily favored small-scale buyers, traders, processors and retailers that usually have much lower operating costs than large-scale enterprises. Evidence shows that monopolistic parastatals and oligopolistic milling firms often have inflated pricing structures that ultimately raise the cost of food to consumers. In contrast, due to low entry costs and more appropriate, lower-cost technology, small-scale traders and processors often operate in highly competitive niche markets and have the ability to supply consumers with staple foods at affordable prices.

As the longer-term positive and negative effects of food aid sales are more fully considered, USAID and its partners must focus on how food is monetized and to whom the food is sold. Where appropriate, USAID must support open and competitive sales as opposed to non-competitive sales. Auctions and tender sales have several advantages over negotiated sales and administered prices:

- Auctions/tender sales eliminate the inherent difficulties in determining a "market price" for monetized food aid;

- Auctions/tender sales offer a degree of transparency that, except in the case of extremely immature markets, can facilitate access to food supplies by small-scale buyers

- Auctions/tender sales offer scope for realizing higher sales prices, thereby generating greater amounts of foreign currency proceeds for CS activities.

It is acknowledged that markets vary and thus auctions and tender sales may not always be feasible. However, efforts must always be made to maximize the openness of the sale, and the CS is required to submit a justification to BHR/FFP as part of its DAP/PAA submissions for monetizations necessitating non-competitive sales.

USAID has considerable experience in working with host countries to monetize Title III food aid through auctions, with lessons learned from over a half-dozen countries. In cases where this expertise might prove valuable, the Title II CS is encouraged to seek guidance from USAID.

VII. COST RECOVERY IN CONTEXT

Cost recovery has been central to the debate surrounding monetization. Revenues generated from Title II commodity sales that are less than the costs incurred in purchasing, shipping, and selling the commodity have drawn the attention of the General Accounting Office, Congress, and others. USAID policy requires that CSs strive to achieve at least full cost recovery (using foreign flag carrier rates) with each and every monetization transaction they conduct. USAID recognizes that full cost recovery is not always achievable and has established a benchmark sales price, below which commodities may not be sold without a waiver by FFP/D. This benchmark serves as an important accountability and reporting tool, but is only one among several criteria for judging the merits of a proposed monetization activity.

Sales prices for monetized commodities determine the amount of resources that will be available for activities aimed at achieving food security impacts. Accordingly, the difference between the costs associated with the purchase and transport of the Title II commodity and the amount of proceeds generated represents the amount of resources not available for programming. In this respect, cost recovery benchmarks act as a measure of accountability, ensuring that monetization resources are used efficiently in terms of U.S. dollars made available by Congress for food security versus U.S. dollars actually spent on food security interventions.

Cost recovery benchmarks are also used to prevent sales that are carried out with little regard for obtaining the "fair market price." To the extent that sales prices are below "fair market" prices for similar transactions in the market, a windfall gain is created. In specific monetizations this may be desirable.[1] In most cases, however, sales below local market prices result in a windfall gain for a particular trader at the expense of programming funds for activities targeted to the food insecure. In addition to the short-term consequences, windfalls for particular traders can lead to an adverse change in the long-term competitive balance in the market and excessive profit for a few individuals. For this reason, the degree to which a sales price is different from (less than) the "fair market" value in the markets where the product is sold must be considered.

Various benchmarks, such as the fair market, C&F, and Free-Alongside-Ship (FAS) values of the commodity to be monetized, have been used for determining sales prices. For example, the fair market value may be very different from either the C&F price or the FAS price. Moreover, the fair market price can only be determined by the interaction of supply and demand forces in open and competitive markets, while Title II commodities are sometimes sold to monopolistic parastatals and oligopolistic traders and processing firms. Clearly, simple observation of "prevailing market prices" may not be realistic since the observation may be based upon a very thin market. Only if demand is perfectly elastic will an additional supply, i.e., the quantity of food aid to be monetized, not translate into a decline in market prices, except in cases where the supply of commodity will be substituting for commercial imports. In these cases, however, the CS should be concerned about creating significant disruptions in vulnerable markets as well as safeguarding usual U.S. marketings under Section 403(h) of P.L. 480. CS are encouraged to work with other donors, traders, partners, U.S. Trade Representatives and embassy Agricultural Trade Attaches where appropriate.

The difficulties outlined above reaffirm that there are often trade-offs involved in terms of recovering costs and achieving food security impacts through the process of monetization. Cost recovery is therefore one of several factors to consider when determining whether or not to

[1] In the case of a "closed monetization," specific vulnerable consumers are identified who are eligible to receive food at prices below market values. The approach is analogous to free food distributions in the sense that it is necessary to identify a specific target group and usually necessary to fix the rations. The process of charging a fixed sum for the food is felt by some programmers to be significant in terms of dignity and the ability of specific communities to raise funds for projects in which they feel a certain ownership.

monetize. Sales below the cost recovery benchmark must be justified through the identification of measurable food security impacts that are unique to the supply and/or sale of food as opposed to cash. The cost recovery benchmark, which is discussed in detail in the Implementation Guidelines section of this document, will be:

> 80% of the C&F value, using the FAS quotation provided by FFP at the time of the call forward, the foreign flag rate, plus port clearing and handling costs and duties, estimated transport costs to move the commodity to the point of sale, and expenses associated with marketing the commodity, or 100% of FAS, whichever is greater.

VIII. REVIEW AND EVALUATION CRITERIA[2]

Proposal approval containing a monetization request will be based primarily upon the anticipated measured impacts on food security. The following criteria will provide the basis for review and evaluation of monetization requests in addition to the criteria in the DAP/PAA and Emergency Guidelines:

1. Assurance that the monetization proceeds will be used to support activities that are expected to achieve demonstrable impacts on food security, as defined by USAID's *Food Aid and Food Security Policy* paper and measured using approved indicators;

2. Assurance that the monetization meets all of the requirements of a Bellmon Determination;

3 . Certification that the amount of currency generated in the monetization transaction(s) will meet or exceed the cost recovery benchmark.

IX. MONETIZATION IN EMERGENCY SITUATIONS

Monetization of food aid in emergency situations is normally supportive of (a) enhancing access to food by vulnerable groups, and (b) generating funds supportive of emergency food activities. Monetization of emergency food aid must be guided by the criteria set forth in Section VIII of this manual. If the criteria cannot be satisfied due to the nature of the emergency, then the FFP/D must make the determination that the benefits of the specific monetization merit a waiver of the Section VIII criteria.

In emergency situations, the monetization of food aid should demonstrate that monetization offers the best option for satisfying the nutritional needs of targeted vulnerable groups. Situations where monetization may be appropriate include small-scale sales in drought-affected villages where surrounding farm families cannot grow enough to support the non-farm community. Other situations may occur wherein small-scale monetization can facilitate the re-establishment of a distribution channel closed by war or natural disaster. Finally, the sale of food aid to cover costs

[2] The same criteria will be used in the review and evaluation of full or 100-percent monetization requests as in those proposals that include both monetization and direct distribution components.

of moving commodities to targeted vulnerable groups may have a more effective and developmental effect than the direct expenditure of foreign currency.

X. THIRD-COUNTRY MONETIZATION

BHR/FFP is still in an exploratory period regarding third country monetization. These types of transactions will be reviewed in the next year to see where they have succeeded and what lessons can be learned and best practices developed.

Third-country monetization requests have become more frequent as monetization in smaller markets are not always feasible. CSs are encouraged however to make every effort to monetize within the country in which they are working. Monetizations in third countries require additional input from many sectors and are often more difficult to piece together. Most of the third country monetizations to date have been successful, but the amount of work necessary to succeed can be more intensive than monetization in an activity country.

CS's should note that third country monetizations are subject to the same review and evaluation criteria as identified in Section VIII above. Prior to developing a proposal involving third-country monetization, the CS should confirm with FFP those LIFDC countries within the region that would be eligible recipients of the monetized commodities. CSs should consult the Monetization Field Manual's Implementation Guidelines, Section XI, Third- Country Monetization for additional information.

TITLE II MONETIZATION

IMPLEMENTATION GUIDELINES

I. MEASUREMENTS COSTS

USAID requires that CSs strive to achieve full cost recovery with each and every monetization transaction they conduct. The following costs must be included when determining the cost recovery of a Title II monetization: the cost of purchasing the commodities in the U.S.; commercial ocean freight for foreign flag vessels; inland transport for landlocked countries; port clearing and duty; inland transportation to the point of sale; and marketing. Guidelines for measuring these costs are provided below.

A. U.S. Commodity Procurement

Two features of U.S. commodity markets have implications on the procurement costs of Title II commodities. First, in general, the specific commodities procured for Title II food assistance do not have one defined price in port position for a specific delivery period unless a transaction is completed. However, public information is available that provides an indication of where these markets would trade if orders were placed. Second, markets for specific commodities vary over time and will depend on the month that the commodity is to be delivered. In this context, there are three distinct types of price information that CSs are required to obtain at different stages of a monetization process.

1. Price Indications

Price indications are approximate prices of commodities in U.S. port position. They may be provided without reference to commodity specification and grade and must be used as the name implies--as indications. These numbers are useful in determining how local prices compare in a general sense with U.S. prices and in tracking changes in these relative prices.

Price indications must be obtained periodically during the preparation of a market analysis and monetization budget proposal. Indications are therefore important during the early stages of the monetization design to determine if a monetization is possible. They must not be used to determine whether or not to proceed with a monetization call forward request.

The Internet is a recommended resource for obtaining price indications. Some useful web sites include:

ftp://ftp.fsa.usda.gov/public/export/default.htm
ftp://ftp.fsa.usda.gov/public/grain/default.htm
http://www.fas.usda.gov (and links to related sits)

Hard Red Winter Wheat (HRW) prices from Kansas City Board of Trade:

http://www.kcbt.com/dgpsum.htm
http://www.ams.usda.gov/mncs/mn_reports/sj_gr710.txt

Hard Red Spring Wheat (HRS) and Soft White Wheat (SWW) from the Minneapolis Grain Exchange:

http://quotewatch.com/exchanges/mgex.html
http://www.mgex.com/wheat/shtfut.htm
http://www.ams.usda.gov/mncs/mn_reports/ws_gr710.txt

Soft Red Winter Wheat (SRW) from the Chicago Board of Trade:

http://quotewatch.com/exchanges/cbot.html
http://www.ams.usda.gov/mncs/mn_reports/ws_gr710.txt

Soybean, Soybean oil, Soybean Meal from the Chicago Board of Trade:

http://quotewatch.com/exchanges/cbot.html
http://www.ams.usda.gov/mncs/mn_reports/ws_gr711.txt

Corn/Maize (Yellow) from the Chicago Board of Trade

http://quotewatch.com/exchanges/cbot.html
http://www.ams.usda.gov/mncs/mn_reports/ws_gr711.txt

Sunflower Oil from USDA Market News

gopher://shelley.ca.uky.edu//00.agwx/usr/markets/usda/MSGR851

Corn, Soybeans, SRW, HRW, DNS, SWW:

USDA Market News (for FAS export U.S. port prices):

gopher://shelley.ca.uky.edu:70/00/.agwx/usr/markets/usda/jogr850

USDA Market News (Missouri Department of Agriculture News) for spot and short-term futures prices:

gopher://shelley.ca.uky.edu:70/00/.agwx/usr/markets/usda/sjgr850

On U.S. commodity exhanges, grains are traded in bushels (Bu.), vegetable oil is traded in pounds (L.b.) and some commodities are traded in hundredweight (Cwt.) The measurements below are from the USDA, Economics Statistics, and Cooperative Service Statistical Bulletin titled "Conversion Factors and Weights and Measures," and can be used to compute the MT value for the information provided by the above Internet sites:

Bushel (Bu.) Weights:	1 Bushel (Wheat/Soybeans) = 60 Lbs. 1 Bushel (Corn/Sorghum) = 56 Lbs.
Bushel to Metric Tons:	36.743 Bushels (Wheat/Soybeans) = 1 Metric Ton (MT) 39.368 Bushels (Corn/Sorghum) = 1 Metric Ton (MT)
Hundredweight (Cwt.)	1 Cwt. = 100 Lbs. 1 MT = 22.0462 Cwt.

2. Price Quotes

Price quotes are approximate values for a specific commodity for delivery in a specific time frame. As such, they require more time to be developed and must be developed for each individual monetization. A price quote must be obtained at the time of the call forward from BHR/FFP/POD.

BHR/FFP/POD will provide a written price quote within three working days after receipt from a CS of a request for such a price quote. The CS's request must be in writing and include the commodity specifications and delivery time frame. This FAS price quote must replace the price indications obtained during the market analysis and proposal development stages and must be used in determining cost recovery.

3. Invoiced Prices

Invoiced prices are the actual prices identified on shipping documents of commodities at the time that the purchase was made in the U.S. Except in unusual circumstances, this price will be different from price quotes received at the time of the call forward. CS must still use the FAS price quotation in determining cost recovery.

B. Ocean Freight and Inland Transport for Landlocked Countries

The Merchant Marine Act of 1936, as amended, requires that 75 percent of Title II food assistance be shipped on U.S. flag vessels. These U.S. shipping costs usually exceed the costs of non-U.S.-flag shipments. In recognition that this requirement is a deviation from standard commercial practices and would make cost recovery more difficult to achieve, estimated shipment costs of ocean freight on a foreign flag carrier, as opposed to the higher U.S. flag rates, will be used for both budgeting and reporting purposes.

Estimated non-U.S.-flag rates must be obtained from the CS's freight forwarding agent during proposal preparation and at the time of the call forward. At the time of the call forward, the CS must provide BHR/FFP/POD with the certification of sales price along with the freight indication in support of the call forward.

C. Cost Recovery Benchmark

Realizing that full cost recovery may not be attainable in all situations, FFP has, for the time being, established a more accommodative cost recovery benchmark. The benchmark is set at 80 percent of the C&F value, using the FAS quotation provided by FFP at the time of the call forward, the foreign flag rate, plus port clearing and handling costs and duties, estimated transport costs to move the commodity to the point of sale, and expenses associated with marketing the commodity, or 100 percent of FAS, whichever is greater.

II. DEVELOPMENT OF A MONETIZATION REQUEST

Full and partial monetization requests are considered integral parts of Title II emergency and non-emergency activities. Accordingly, when monetization is requested, the requests must always be included as part of the submission. In addition to this field manual, the CS must refer to Regulation 11 as well as the guidelines for the preparation of Title II development or emergency proposals, which are published annually by BHR/FFP, for instructions regarding the submission of monetization requests.

Monetization requires an ongoing understanding of the local market. The following are the key elements, in addition to the market analysis section of the Bellmon Determination, which must be included in the monetization component of a Title II proposal.

A. Justification for Monetization

Justify the appropriateness of monetization by examining, as appropriate, the anticipated impacts of the end-use of the funds, the amount of funds to be generated, the supply of food or sale itself, and the potential for development of local markets.

1. End-Use Justification

   Explain in detail the specific uses of the foreign currency resources by Title II intervention. State which interventions supported by foreign currency proceeds involve direct distribution of Title II commodities and which do not. Provide a percentage breakdown of the amount of foreign currency proceeds that support each activity intervention.

   Note: Title II monetization must be included as a funding source in the comprehensive budget. The specific foreign currency uses described above must be clearly linked to specific monetization budget line items. The total amount of foreign currency budgeted must be used to determine the amount of tonnage needed. In other words, there should be a direct correlation between the budget requirements and the amount specified for monetization on the AER.

2. Cost Recovery Justification

   Justify the monetization on the basis of the amount of funding to be made available for programming as compared to the costs incurred in carrying out the monetization. In the case where the monetization does not have objectives beyond raising cash to support Title II activities, this must be stated explicitly. If the revenues generated by the sale are expected to be less than the cost recovery benchmark, the difference must be justified on the basis of food security impacts. See Section V.B.

3. Supply Justification

   If the monetization is justified on the basis of the proposed food security impact of the sale, identify the potential supply effects from the monetization, including the impact of the additional supply of food in the market, as well as the effects anticipated from the sales process. Identify all features of the monetization that have value but are not captured in the cost recovery equation.

4. Market Development Justification

   Monetization can be an effective tool for contributing to the development of local markets by broadening the participation in commodity sales to include small- to medium-sized traders and/or those traders who may not have traditionally had access to commercial opportunities. Strategies for strengthening local market capacity include reducing barriers to entry for smaller traders, developing appropriate payment plans, and facilitating the movement of commodities into rural areas.

   Justification on the basis of market development must include a profile of the commercial environment and strategies to be used to increase participation, as well as targets for measuring success.

   Using a chart or table form, identify the specific objectives of the monetization sale and the benchmarks and indicators that will be used to measure progress against these objectives.

B. Preliminary Proposed Mechanics of the Monetization

1. Describe the rationale for the commodity or commodities chosen for monetization. What is the end-use of the commodity chosen? What are possible alternatives to the commodity chosen?

2. Identify and justify the proposed time frame for the sale. Provide seasonal prices and harvest schedules where relevant and available and identify other key price determining factors.

3. Identify and justify the proposed location of the monetization. In doing so, identify regional prices for the commodity and describe the market structure.

4. Describe and justify the sales methodology, particularly in relation to the proposed objectives of the monetization and to the existing market structure. Describe the proposed terms of payment. Identify roles, where applicable, of agents and other participants in the sale.

5. Verify that the commodities to be monetized are in demand and not in competition with similar or substitute commodities. State the current sources and approximate amounts of supply of the proposed monetization commodity and its close substitutes, taking into consideration other donor imports and subsidy programs, such as USDA's Export Enhancement Program (EEP). Discuss the volume of commodities proposed for monetization in relation to the size of the market in which the monetization will take place.

6. Describe the storage facilities both at port and inland that will be available in the recipient country when the commodities arrive.

C. Monetization Sales Budget

For proposals that have a monetization component, the CS shall provide a separate monetization sales budget for the purpose of analyzing estimated sales costs versus revenues. Refer to the section of this manual on measuring costs for relevant definitions. For each commodity to be monetized, the budget must include:

1. U.S. Commodity Price Indication ($/MT x amount requested);

2. Estimated Ocean Freight and Inland Transport for Landlocked Countries ($/MT x amount requested);

3. Estimated Internal Transport to the Point of Sale, Duty, Handling, Port Clearing, and Marketing Costs. Break out these costs by line item;

4. Base Costs (sum of 1-3, above);

5. Estimated Sales Revenue plus Projected Interest to be Earned ($/MT x amount requested) + interest;

   Use the estimated sales price ($/MT) of the commodity or a similar commodity in the sales position considered for the monetization. The total amount should correspond to the amount of Title II foreign currency budgeted for in the comprehensive budget; and

6. Preliminary Cost Recovery Estimate - Express item 5 as a percentage of item 4.

D. Sales Proceeds Management

1. Identify the means for mitigating the effects that inflation and currency devaluation might have on the monetization proceeds. Two possible methods include depositing the funds in an interest-bearing account and converting the proceeds to a hard currency.

2. Identify the financial institution in which the sales proceeds are to be deposited and verify that the proceeds will be deposited in a separate interest-bearing account.

3 Describe the monitoring or accounting system that exists to track the receipt, disbursement and expenditure of the foreign currency proceeds. Describe the monitoring role of the Mission in terms of reporting requirements, frequency of reporting, etc.

4. In the case of umbrella monetizations, describe the legal relationship between the lead agent and each participating CS. Attach as an appendix the inter-agency monetization agreement. The agreement should describe the organizational and management framework, including the allocation and disbursement processes and the fee payment schedule, if appropriate.

III. MISSION ROLES AND RESPONSIBILITIES DURING THE DEVELOPMENT OF A MONETIZATION REQUEST[3]

A. Ongoing Technical Support

To the extent possible, Mission technical staff, e.g., agricultural economists, must provide CSs with technical assistance during all stages of the market analysis, fine-tuning, and sales preparations.

B. Bellmon Determination

For the commodities to be monetized, the Mission must provide explicit determination regarding the CS's Bellmon analysis. The USAID Mission must describe its role in analyzing the market in which the monetization will occur. If the CS's Bellmon analysis is rejected, the Mission should explain why. It is not necessary for the CS to provide a disincentive analysis if the Mission or USDA has completed such an analysis for another program that is relevant to the program proposed by the CS.

C. Certification of Cooperating Sponsor Financial and Management Systems

Missions must certify the adequacy of the CS's financial and management systems for carrying out the monetization activity. If there are shortcomings in the CS's financial and management systems, determine whether corrective action can be taken or whether the deficiencies are significant enough to warrant rejection of the activity.

D. Concurrence of Sales Price Analysis

Missions must provide explicit concurrence (or rejection) of the sales price analysis undertaken by the CS. If the analysis is rejected, the Mission must provide reasons for the rejection.

E. Third Country Monetizations

Benefiting Missions are responsible for assisting CSs in their third country monetization requests. This may include, but not be limited to: 1). Providing technical assistance in carrying out a Bellmon review in the third country;
2). Assisting the CS with third country clearance (ie. Bellmon Determination and proceed expatriation); 3). Assisting CSs in UMR process; 4). FFP encourages CSs and benefiting Missions to communicate with the monetization country Mission or Embassy to alert them of pending third country monetization requests. In instances where the benefiting mission is unable to perform these functions they may request FFP/W to assist. FFP assistance will be based on management capacity and funding availability to provide

[3] In countries where there are no Missions operating, or no Mission has a twinning responsibility, the term "Mission(s)" in Sections III B, C, and D will be replaced with "BHR/FFP."

the necessary technical assistance.

IV. REVIEW AND APPROVAL OF MONETIZATION REQUESTS

A. Review and Approval Process

In general, review and approval of monetization requests will be subject to the guidance provided by BHR/FFP for the review and approval of all Title II proposal submissions.

In the case of multi-year approvals for development activities, as long as the objectives unique to the monetization, the commodity choice, and the mechanics of the monetization remain the same, annual approval of commodities for monetization is subject to submission of the following:

- monetization sales budget, as described in Section II.C. above;
- Bellmon Update, as described in Section II.B.5.-6. above; and
- comprehensive budget, with foreign currency pipeline analysis, as described in annual Title II guidelines and referenced in Section II.A.1. above.

  If the objectives unique to the monetization, commodity choice, or the mechanics of the monetization have changed, a comprehensive monetization request, as outlined in Section II., must be submitted for Mission (if applicable) and BHR/FFP review and approval.

  Approval of monetization requests equates to recognition that the monetization is conceptually possible. Between the time of the approval and the time of the call forward request for monetization, actions must be taken by the CS to refine the proposed mechanics of the monetization and verify whether the anticipated sales price will meet the cost recovery benchmark.

B. Review and Evaluation Criteria[4]

As noted in the Policy Framework section of this document, the merits of all monetization requests will be judged against the following criteria, in addition to those stated in the DAP/PAA or emergency proposal guidance:

1. Assurance that the monetization proceeds will be used to support activities that are expected to achieve demonstrable effects on food security, as defined by USAID's *Food Aid and Food Security Policy* paper and measured using generic or otherwise approved indicators.

[4] The same criteria will be used in the review and evaluation of full or 100-percent monetization requests as in those proposals that include both monetization and direct distribution components.

2. Assurance that the monetization will not create disincentives to local production or marketing of the commodity to be monetized or its substitutes..

3. Certification that the amount of currency to be generated in the monetization transaction(s) will meet or exceed the cost recovery benchmark[5].

V. PROCEDURES FOR CALL FORWARD AND PRICE QUOTE REQUESTS

Approval of calls forward for monetization will be contingent upon the provision of updated market information and confirmation that the sales price is expected to be at or above the required benchmark. Monetization calls forward for sales anticipated to be below the cost recovery benchmark will not be processed unless a waiver is signed by FFP/D.

A. Information Required for Approval of a Monetization Call Forward

At the time of the call forward request, the following information must be submitted to BHR/FFP/POD:

- clear commodity specifications;
- for negotiated sales:
  - -- written verification that a signed contract is in place and confirmation of the negotiated sales price, or
  - -- CS certification of the expected sales price, which must meet or exceed the cost recovery benchmark;
- for tender sales/auctions:
  - -- adequate evidence that the market is competitive or can be made so;
  - -- CS certification of the estimated sales price, which must meet or exceed the cost recovery benchmark;
- Mission concurrence on the call forward request.

B. Waiver Requests

Where a CS does not expect a monetization to meet or exceed the cost recovery benchmark, but rather proposes to conduct the monetization because of its anticipated food security impact, the CS must submit a written waiver request to the FFP/D for approval of the monetization call forward for a sale price below the cost recovery benchmark. CS headquarters and USAID Missions will be notified of decisions on waivers within 15 days after receipt of the written request.

[5] When a monetization is not expected to meet or exceed the cost recovery benchmark, a request for a waiver must be submitted to and approved by the Director of Food for Peace (See Section V.B. below regarding Waiver Requests. The request must justify the monetization based on its anticipated food security impact).

VI. THE SALE

A. Transfer of Title to Cooperating Sponsor (Per Reg. 211.4(b)(i))

Title to commodities for monetization passes to the CS at the time and place of delivery FAS at U.S. ports. The CS is responsible for all arrangements in connection with the receipt, storage and maintenance of the commodities for monetization from the time of delivery at the U.S. port to the time of delivery to the purchaser. This includes transportation of the commodities overland to landlocked countries. Unless the CS has requested USDA to perform the discharge surveys, the CS must arrange to have an independent surveyor attend the discharge of the commodities and may, at its option, engage an independent surveyor to supervise clearance and delivery of the cargo from customs or port areas to the purchaser and to issue appropriate delivery survey reports. The CS's commodity monitoring responsibilities cease once the full amount of the agreed purchase price has been deposited into the CS's account and title to the commodities has passed to the purchasers or other third parties.

B. Performance Bonds

The CS should obtain a performance bond prior to submitting a call forward to BHR/FFP/POD. The performance bond should equal at least 10 percent of the expected sales price and be denominated in the currency in which the sale will take place. The bond should take the form of an irrevocable letter of credit (or similar instrument, in accordance with local practices) and guarantee payment to the CS of the amount of the bond in the event that the buyer of the Title II commodities fails to perform in accordance with the sales agreement.

Any proceeds generated from the payment of a performance bond shall be treated as program income and must be applied to the approved budget for Title II activities.

C. Payment of Duties and Taxes

Title II commodities for monetization may be taxed by the host government, even though taxation is clearly prohibited for commodities imported for direct distribution. The CS may negotiate agreements with host governments which permit the tax-free import of commodities for monetization. USAID only agrees to the payment of such taxes if the monetization price is sufficiently high to recover all costs, including commodity value and freight plus the tax itself.

USAID Missions and CSs must carefully consider the effects of payment or non-payment of taxes in terms of limiting the proceeds available for programming, in the case of the former, and disrupting the local market, in the case of the latter. Any waiver of duties or taxes should result in a higher sales price rather than a windfall to the buyer. In countries where tax practices are deemed problematic, the USAID Mission and CS are encouraged to negotiate with the host country to establish an agreement whereby taxes and duties would be charged, as in a commercial transaction, but the Title II CS would be allowed to retain those taxes and duties as a host country contribution to the program.

D. Markings

Commodities for monetization will arrive in country with the following "abbreviated markings": description of contents, net weight, and USAID contract number. The phrase "not to be sold or exchanged" will not appear. The buyer may subsequently repackage or label, at its own cost, without restriction by USAID or the Cooperating Sponsor.

If a CS has special marking requirements, the requirements must be specified in the proposal, if possible, as well as at the time of the call forward.

E. Sales Agreement

The CS is responsible for ensuring that a comprehensive and legally acceptable sales contract is in place. Although sales agreements will vary according to country circumstances, the following essential provisions must be included:

1. Full commodity specifications and tonnage;

2. Agreed total sales price. A discount range should be included in the agreement in order to prevent failure of performance on the part of the buyer in the event that the commodities do not meet the exact specifications as stated in the call forward;

3. How and when payment(s) will be made, amount(s) of payment(s), terms of payment(s) (including a description of the terms), if applicable, exchange rate used (including whether it is a market-based rate) and when used (e.g., at the time of payment, at the time of signing the agreement), and a guarantee that payment will take place. In no case should title to or possession of the commodities pass to the buyer until payment in full has been received by the CS;

4. Statement of purchaser's capability to take delivery, properly store and successfully market the commodities in-country;

5. Stipulation that the purchaser will not export commodities or products thereof;

6. Agreement by purchaser, having accepted the commodities when discharged at the port of entry, not to raise claims, thereafter, about the "wholesomeness" or "fitness" of the commodities; and

7. Date of sale.

VII. REPORTING REQUIREMENTS

A. Sales Price and Revenue Analysis

Within 30 days after the sale, CS field offices are required to report in writing to the USAID Mission the actual sales price in comparison to the cost recovery benchmark. Where there is no USAID or REDSO presence, CS shall provide a report to BHR/FFP/POD. Appendix C contains a standardized format for reporting this information. In the event that CS fails to achieve cost recovery, USAID Mission shall report back to FFP/D the circumstances regarding the loss. The CS is also required to report actual revenues generated in comparison to approved budget requirements, in their PAA and CS's Annual Results Report (R2).

In the case of numerous sales throughout the year, reporting of sales prices may be done on a less frequent basis, when approved by USAID.

B. Financial Reporting

Consistent with Regulation 11, Section 211.5(l), the CS must provide a written report of all Title II monetization activities to USAID/W on an annual basis. This report must include information on the receipt and disbursement of both monetized proceeds and program income by the CS and any sub-recipients. The report must also show the source of funds, by country, and how the funds were used. The report must be submitted as part of the CS's Annual Results Report (R2).

VIII. MANAGEMENT AND ACCOUNTABILITY

A. Maintenance of Proceeds

See Section II.D. of this document.

B. Funding Shortfalls and Surpluses Due to Difference Between Revenues Generated and Approved Monetization Budget Requirements

1. Surpluses

In the event a CS generates a larger amount of monetized proceeds than expected during any activity year, the CS must include such surpluses in the annual report submitted to USAID/W. Any surplus funds may not be utilized without written approval of FFP/W. The CS is encouraged to discuss the surplus in the annual report indicating how the surplus funds could be incorporated in the overall activity plan. Possibilities include a reduction in out-year commodity requirements, proposed modification (expansion) of activities, or, consistent with Regulation 11, Section 211.11(b), at expiration of the program, transfer of surplus monetized proceeds to another approved activity. In any event, monetized proceeds above the level approved in the DAP/PAA budget, may not be utilized by the CS without the written approval of FFP/W.

2. Losses

Commodity losses that occur during transport of the commodities are governed by Section 211.9 of Regulation 11. For losses resulting from an unexpected drop in commodity prices or from any loss due to currency fluctuation that are expected to have a negative programmatic impact, the CS must submit a written report detailing the circumstances of the loss. The CS may request additional commodities to compensate for the shortfall of monetization proceeds resulting from the loss. Provision of commodities is not automatic and consideration will be given only after written justification from CS is provided. Limitation of funds and CS responsibility for the loss may be a factor in BHR/FFP's consideration of any replacement.

C. Maintenance of Currency Pipeline

The guidelines for preparing new DAPs specify that up to a five month pipeline is allowed to be carried over from one fiscal year to the next. However, funding carry-over necessary for program implementation depends on the activity being implemented. If five months of pipeline is insufficient, then the CS will be required to justify additional carry-over. A pipeline analysis will be required with the submission of the PAA and, if deemed necessary by FFP, at the time of a call forward.

D. Roles and Responsibilities of USAID Missions During Activity Implementation

Due to the complex nature of monetization transactions, Missions may be required to take on responsibilities that are in addition to those spelled out in Regulation 11.

Missions are responsible for receiving and reviewing CS reports regarding monetization. The following reports shall be used in reporting on monetization: Appendix C; CS's Results Report (R2); and resource requests (PAA).

Missions must report back to FFP/D circumstances regarding CSs not achieving at least benchmark recovery on their monetization of Title II commodities.

E. Roles and Responsibilities of Cooperating Sponsors During Activity Implementation

- The CS is required to notify BHR/FFP of shifts of 10 percent or more between line items in its approved budgets.
- Within 30 days of the completion of the sale, the CS is required to report to USAID Mission or BHR/FFP/POD where there is no US government presence, at a minimum, the information listed below. (See Appendix C format for reporting the details of a monetization activity.)

1. the actual price at which the commodity was sold;
2. total sales revenue, which must be reported in U.S. dollars; and
3. the quantity sold, reported in metric tons.

In the case of numerous sales throughout the year, arrangements can be made to report this information on a less frequent basis.

F. Roles and Responsibilities of BHR/FFP During Activity Implementation

- For price quotation requests which are received in writing and indicate commodity specifications and delivery time frame, provide price quotes within three working days;
- Respond to all regulatory requirements such as non-U.S. vehicle purchase waivers;
- Review Bellmon updates;

IX. UMBRELLA MONETIZATION

CSs are strongly encouraged to monetize jointly. Umbrella monetization can keep marketing costs and expenses related to analyzing markets contained, avoid duplication of effort, strengthen the ability of CS to negotiate more competitively in the market, and increase the potential for achieving supply impacts stemming from the expertise gained by the lead agent and the additional time and money that can be devoted to this objective. However, in cases where a CS can identify the benefits of conducting an individual monetization rather than an umbrella monetization, USAID will not deny the request of the CS to monetize individually.

A. Role of Umbrella Sales Agent

The role of the Sales Agent is generally limited to preparing for and conducting the sale of commodities. The Agent's responsibility terminates when the proceeds of the sale have been deposited into the individual CS's bank accounts.

B. Joint Monetization Agreement

A Joint Monetization Agreement detailing the terms and conditions of the umbrella monetization must be executed by each of the participating CSs and submitted to FFP, where possible, with each of the CS's DAPs but otherwise prior to the first call forward.

C. Monetization Committee

It is recommended that a Monetization Committee be established in all countries where two or more CSs intend to conduct a monetization, whether jointly or on an individual basis. The committee must be comprised of representatives from the CSs and the Mission, preferably the FFP Officer, as well as other individuals with monetization or market expertise. Mission representatives will participate only in a non-voting capacity.

X. COORDINATION WITH OTHER DONOR AND DONOR SUBSIDY PROGRAMS

In countries where more than one donor or CS is importing food aid, Missions must facilitate regular coordination of activities and exchanges of information, especially with regard to market information. The CS should actively participate in coordination efforts.

XI. THIRD-COUNTRY MONETIZATION

Third country monetizations are subject to the same review and evaluation criteria as identified in Section VIII of the Policy Framework section of this manual. In addtion the following are required prior to FFP/W approval:

1. CS's must address the following order of precedence of countries in their monetization request:

    A. CS's Activity Country

    B. All LIFDCs in the region.

    C. All non-LIFDCs in the region.

The CS must first demonstrate that commodity sales, in the country in which they have their activity, are impracticable.

Once the above is determined then the CS may consider sales in other LIFDCs in the region. Special consideration will be given to a CSs who determine that the benefits from the sale of commodities in a third country, LIFDC, will be greater than the benefits that would accrue to the CS's Activity Country.

Only after all LIFDCs in the region have been considered, may the CS propose monetizations in non-LIFDCs. For a current list of LIFDCs, contact FFP/W.

2. The USAID Mission operating in the country where the monetization sale takes place has the responsibility of reviewing and either concurring with or disapproving the CS’s market and storage analysis, i.e, making the Bellmon Determination. If there is no Mission, the determination will be made by FFP/W.

3. CS shall work with the USAID Mission, in the country in which the monetization of commodities occurs, to ensure that the third country government does not object to proceeds generated under the sale, being transferred out of the country to fund activities in the CS’s proposal.

4. Third country monetizations are subject to Usual Marketing Requirements. CS's monetization request(s) for third country monetization will be evaluated by FFP/W in coordination with USDA to determine if further UMR analysis is required. Potential UMR limitations will be reviewed by USAID, USDA and the Department of State. FFP/W will notify CSs regarding the determination.

5. Benefiting Missions shall play a role in assisting the third country Mission in providing all clearances. (See Implementation Section, III, E.)

6. CS should be aware that monetization proceeds generated in a third country can be converted to a hard currency for transfer to the country of program activity.

XII. TITLE II ACTIVITY CLOSE-OUT

Refer to Title II Close-out Plan Guidance.

Appendix A - Market Analysis Overview

Appendix A and B are supplemental to the 1985 Background Paper and Guide to Addressing Bellmon Amendment Concerns on Potential Food Aid Disincentives and Storage.

The CS's market analysis, upon which part of the Mission's Bellmon Determination is based, must attempt to capture potentially significant effects on marketing and production incentives. A complete market analysis will address the following points.

1. Market analysis must consider possible effects on marketing agents as well as producers.

There has been a tendency to focus on the potential disincentive effects on producers, while ignoring the potentially damaging effects on private sector marketing agents who transport, process, distribute and sell a variety of foodstuffs. Even if a given commodity is not produced domestically, private sector marketing agents may buy and sell the commodity and be harmed by sudden price falls.

2. Monetized food aid commonly has an effect on food prices. Market Analysis must seek to understand the magnitude of the price effect.

Market analysis often rests upon the widely held supposition that monetized food aid does not depress domestic prices if it meets a national shortfall. In actuality, whenever local food prices are largely determined by competitive forces, any sale of Title II food aid effectively results in an increase in supply, which then can reduce prices. Whether the resultant fall in price is negligible or whether it is significant depends upon a host of factors.

3. In a market analysis, the amount of food aid to be monetized during a particular time period must be contrasted to the amount of food in local food markets during that time period, not simply to "total domestic consumption or production."

Past market analyses have measured the possible disincentive effects of food aid by comparing the amount of monetized food aid to "total domestic consumption." For example, it has been suggested that disincentive effects may exist only when the amount of food aid exceeds five percent of total domestic consumption for the upcoming year. Such comparisons are very misleading since, in many countries, marketed surplus is a very small proportion of total production and consumption. That is, compared to total consumption, relatively small amounts of a given commodity are marketed. As a result, food markets in developing countries are often "thin" and volatile. This means that small changes in quantities supplied during specific time periods can have a large impact on prices. By extension, monetization of relatively small amounts of food aid can have enormous effects on thin and fragile domestic food markets.

4. Market analysis must consider the timing of flows of food through local markets in determining the potential for any disincentive effect.

Market analysis often ignores the concentrated time frame within which a given CS monetizes food aid. Food markets in developing countries exhibit a predictable pattern in the timing of food flows into the market. A comparison of the amount of food aid that is monetized by a CS during a two- or three-week period to a nation's total annual food consumption may present a deceptive picture of the likely impact of the infusion of monetized food.

5. Market analysis must demonstrate that monetized food aid will have little impact on incentives for traders to engage in intra-annual storage or on farmers' planting decisions. Above all, monetized food aid should not be viewed as a tool to prevent normal price fluctuations.

Market analysis often contributes to the assumption that food aid monetization can play a valuable price fluctuation "mitigation" role during periods of high food prices that may have a negative effect on the household food security of targeted groups. Often food aid is monetized during the "hungry season"--right before harvest when prices are highest--based upon the assumption that food aid can "stabilize" markets. The hungry season seems to be an appropriate time to monetize food aid. Such monetizations may lead to lower food prices, benefiting consumers. However, monetizing food aid may impair the development of food systems that assure year-round indigenous, locally produced or imported food supplies. Commodity flows may be greatest immediately after harvest, but in most years, sales by producers and middlemen to others in the food system occur throughout the year. However, by monetizing food aid, incentives to private traders to perform valuable storage functions may be severely damaged.

6. Market analysis must consider the possible cross-price effects on substitute commodities.

Market analysis also often ignores potentially high cross-price elasticities of demand when analyzing the effects of the monetization of a particular commodity. In other words, simply because a commodity is not produced domestically does not imply that the monetization of this commodity will have little or no effect on local food markets. Consumers often have an array of food consumption choices and choose among potential substitutes based upon relative prices. Even if wheat is not grown in a particular country, monetization of wheat may have effects on rice prices by inducing people to shift from rice to wheat.

7. Market analysis must consider the aggregate effects of multiple monetizations in a particular country.

Market analysis, when undertaken by a particular Cooperating Sponsor, fails to consider the aggregate effect of monetized or distributed food aid supplied by multiple CSs and other donors. For example, if six CSs are each monetizing 10,000 tons of wheat per year, each CS may independently make the determination that a 10,000-ton monetization has few effects on local incentives, failing to consider the aggregate effects of all six monetizations. To the extent possible, it is recommended that CSs prepare a joint market analysis.

Appendix B - Market Analysis Procedures

A. Introduction

Markets are defined by specialization, trade and usually a medium of exchange. Primary markets, as opposed to secondary or resale markets, represent a delicate balance between producers and consumers. Consumers procure required foodstuffs and producers receive currency (money) representing a promise of future goods or labor. Markets may be controlled by State regulation and intervention or dominated by private trading. In markets dominated by private trade, competition brings products to consumers in a cost effective manner.[6] Maintaining competition over time requires a balance among competitors in terms of access to capital and products.

Monetization potentially has an impact both on the balance between producers and consumers, as measured through market prices, and on the balance among traders, as measured by the participation and degree of competition in the market. In order to understand the impact of monetization on each of these balances, a thorough and ongoing understanding of local markets is required.

The intent of this appendix is to suggest a number of analytical considerations that will help the CS narrow the range of information required to monetize their commodities effectively. For most CSs, it will not be cost effective to understand the entire food market. Therefore, the key will be to understand the broad market setting well enough to recognize possible opportunities, and then to understand individual commodity markets in enough detail to be able to anticipate the effects of intervening.[7]

The steps outlined in this appendix represent one approach to market analysis. It is recommended that the CS consider this material particularly with reference to understanding the food security impacts of monetization. The appendix is not designed to repeat or replace the work of other guides to monetization.

B. Purpose

In broad terms the purpose of market analysis is to determine if there is a niche for monetizing P.L. 480 commodities in a particular country. A niche for monetization will depend on the expected returns from the sale and on the food security impacts of adding food to the market. These effects of monetizing food aid should be considered apart from the anticipated use of the proceeds for developmental purposes. USAID will look favorably upon those proposals that demonstrate a clear understanding of markets. However, it is hoped that the driving motivation in studying markets will be a recognition by the CS that market systems have profound implications for vulnerable people and that good food programming depends on an understanding of local markets.

In addition to the generation of proceeds for developmental activities (returns from the sale),

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[6]Markets that are less competitive generally result in higher prices paid by consumers.

[7]For example, see Food Aid Management's *Monetizing Food Aid - 1993 - A Guide for PVOs* and Save the Children, *Monetization Implementation Manual*, February 1993. For CSs wanting further research-related material on market analysis, see Scarborough, V. and Kydd, J. (1992) *Economic Analysis of Agricultural Markets: a Manual*, Chatham U.K.: National Resources Institute.

monetizations may save foreign exchange for the host country. This can have the effect of supporting the value of the currency and enhance government revenues, depending on the use of the proceeds. Exchange savings may come at the expense of usual commercial imports or, in the case of a crop short-fall, replace one-time purchases. This section will not focus on these aspects of monetization, i.e., exchange savings and usual commercial imports, which are treated in more detail in Appendix A - Market Analysis Overview. Rather, we will consider here the more narrow issue of how monetized food aid can be used to develop markets.

Monetized food aid can be used to further the development of agricultural and food markets when the sales methodology directly affects the structure of the market. Although perhaps difficult to target in terms of market structural effects, large quantities of food aid have the potential to affect markets in dramatic ways, especially if a program continues over several years. Demonstration of potential food security impacts of a monetization typically requires the identification of a market inefficiency. There are several types of market inefficiencies that one frequently encounters in a developing country, which usually translate into higher costs for the marketed product. Marketing costs may be high due to: insufficient investment, a small number of traders, quasi-monopolistic or oligopolistic practices, the irregular or seasonal functioning of the market, a paucity of supply or limited demand. These, among other conditions, are common characteristics of developing country markets which food aid monetizations may seek to address. Food aid monetizations may induce traders to come into the market and invest; they may supply needed commodity on a regular basis; they may broaden the extent of the market and assure better means of payment and settlement of accounts. The CS will need to understand how the market has failed and how a monetization will have an impact on redressing this situation. In short, in order to have a food security impact, the CS must identify a problem and identify how U.S. resources will have a positive impact on the solution via the monetization.

In addition to determining opportunities, market analysis will provide the CS with guidance on how to execute the monetization. Market analysis will identify suggested methods of determining the price, specific requirements of the commodity, timing considerations, and potential risks. The data in the market analysis will provide some of the information required to do a Bellmon Determination[8] properly. Ultimately, most management decisions taken during the successful execution will be based on information obtained in the market analysis.

[8] In a Bellmon Determination, the CS is required to provide enough information to the Mission to demonstrate that a commodity is suitable for monetization (or distribution) in the recipient country, adequate storage is available in the recipient country, and import of the commodity will not result in a substantial disincentive to or interfere with domestic production or commercial marketing of the commodity in that country.

C. Suggested Procedures

1. Information sources - Market analysis will inevitably involve many interviews with market participants, including importers as well as domestic and off-shore traders. This process is often less intimidating than it sounds. Off-shore suppliers and traders can be contacted by phone and requested to give price quotes. The CS often purchases foods in the region and may have these contacts on file. With regard to local traders, establishing a large network of contacts will help the CS to ensure that it is provided with fair and accurate price quotes. In addition to the private traders, WFP, FEWS, GIEWS, and local government agencies often track prices in a systematic way. (Pointer: Know your product - Suppliers will respect a caller who knows exactly what product is being priced. For example, wheat flour has many different specifications. Ask local bakers who may be using the flour what specs they require and then price on the basis of these specs.)

2. Short list commodities - The first step in looking for a niche is to ask the basic food questions: Which foods are eaten? Which foods are eaten by vulnerable people? Of the commodities consumed, which ones are typically a part of the U.S. P.L. 480 food basket? All commodities available and consumed locally should be initially placed on the short list.

3. Prioritize the short list - To prioritize the short list, two quick tests should be applied.

> **a. Cost Recovery** - Create a list of FAS prices for P.L. 480 type commodities. Suggested web sites for obtaining commodity price indications are listed in the Implementation Guidelines section of this manual. Add to these price indications the costs included in the cost recovery benchmark calculation to obtain an estimate of the costs of each commodity. Obtain current wholesale price estimates in the market in which a sale would be considered. Compare these prices to those calculated from the P.L. 480 program.
>
> **b. Food Security** - Commodities that are eaten primarily by the poor may be marketed in a significantly different manner than those purchased by the wealthier population. Urban and rural markets may also be organized in different manners as might those for particular commodities. It is importamt to know how the market for the particular commodity being monetized is organized and how the monetization might potentially enhance food security through developing that market.

Note that the two tests will often yield opposing results. For example, the cost recovery test might indicate advantageous pricing for a certain commodity while market structure (demand, imports, target population and target market) might indicate another.

4. Rationale for more information - Depending on whether the commodity meets the criteria of the cost recovery test or the food security test, the CS will require different additional information.

If the commodity is prioritized based on the initial impression that sales will meet or exceed the cost recovery benchmark, then the fundamental questions are whether or not the initial impression was correct and whether or not the prices can be expected to remain stable long enough to execute the sale. Judgments about price stability must rely upon an understanding of the forces driving current prices.

If a commodity is prioritized because it is eaten by the poor and the CS wants its food to have a positive impact on food security, similar information is collected, but it is used differently. For example, market structure information should be able to explain why poor consumers are charged the prices that they are and suggest ways to intervene that will reduce poor consumers' food bills in a sustainable manner. All price data as well as seasonality are viewed in terms of whether or not there is a problem for vulnerable people and whether or not a strategic sale has a reasonable probability of addressing the problem.

5. Understand the Traditional Food Market Channel - For imported goods, determine import parity prices.[9] To calculate these, it may be possible to find out what is being paid by importers. Alternatively, it may be necessary to phone suppliers at the point of origin to obtain quotes. Freight costs are available through USAID, the International Wheat Council, and many freight forwarders or brokers. Once in port, the goods may incur import duties and taxes, port handling charges, port clearance fees, and inland transportation costs to the first market. These fees should all be estimated. The prices at major terminal markets en route from producer to consumer should be determined. For processed goods, the processing margin should be estimated. Processing margins usually involve a margin for costs and a margin to recognize that not all of the raw product is turned into final product. From central markets, the goods will go to retailers. Retail prices should also be tracked.

For domestically produced goods, the channel is similar except that the import prices are replaced with farm prices. Farmers will be able to tell if the goods are commonly marketed at harvest or throughout the year.

6. Compare Price Margins to Costs - Using prices from point of supply to the consumer, two simple analyses are possible. First, the difference between prices at consecutive stages is referred to as the price margin. Calculate the price margins. Compare these margins to known costs such as transport, storage, and processing costs. Second, compare these margins to the costs that would be incurred in getting the commodity to that stage in the food channel. This analysis may help to define where to sell and whether to send the raw or a finished product.

7. Understand Market Structure - Interview traders and processors to determine the degree of competition and any government regulations that may be in place at each stage of the market channel. Particular attention should be paid to those stages where margins appear to exceed the estimated costs plus a reasonable profit. For monetizations motivated by returns, the objective is to get a sense of whether the factors causing the price spread are cyclical or anomalous. For monetizations motivated primarily by a desire to have an impact on food security, the intent is to understand whether or not it would be possible to improve the performance of the market. (Pointer: Interview the people who sell to and buy from a particular segment of the market to get a further sense of the degree to which competition may be imperfect.)

8. Understand the Foreign Exchange Market - When imported commodities are considered, review the foreign exchange market. Is there a restriction on foreign exchange? Is there a parallel or street market for exchange that is different from the official rate? If there is a margin, what is

[9] Import parity is understood to be the cost of importing <u>comparable food products</u> from the least cost supplier. It should be noted that this price will likely be less than the full cost of bringing commodities from the U.S. through the P.L. 480 program.

the spread between official rates and parallel rates? Are most or all goods available with local currency or is it necessary to use foreign exchange to purchase a wide cross section of goods? Are there regular devaluations? For monetizations executed with the intent to maximize returns, restriction on foreign exchange is often one of the factors that makes monetized goods attractive. For monetizations executed with the intent to improve food security, a shortage of foreign exchange is often cited as the reason that the monetization is important for the food security of the country. In order to make a sound food security argument, it will be important to think about whether or not the imports are additional or if the ability to purchase in local currency is simply creating a windfall gain for a trader.

9. Learning Lessons from Past Prices - Determine historical prices when possible. Weekly or monthly price series in central markets will often be available from FEWS, GIEWS, WFP, or a local government ministry. This information might also be available from USAID in countries where the agency sponsors market information projects. Plot weekly or monthly data for the past year to determine seasonality. For monetizations designed to generate the maximum amount of foreign currency proceeds, the objective is to determine whether recent price fluctuations/ stability can be expected to continue in the near future. For monetizations designed to have an impact on food security, the objective would be to determine unacceptable price swings and empower more vulnerable groups to become involved in the market through a monetization which would help to smooth radical price swings in the future. In this case, the historical prices may form a baseline for reporting.

10. Understand the Size of the Market - Obtain an estimate of the size of the commercial market. This information will help predict the degree to which prices will be sensitive to additional supplies. USDA and FEWS are likely to have the relevant information. For monetizations taking place outside the capital or port, this information may have to be estimated for the specific location. Traders can be interviewed and local wholesale markets observed. This information forms the base for the Usual Market Requirements.

11. Confirm the Reasons for Short Listing - Once market analysis has proceeded to this stage, the CS should be in a position to answer the following questions:

a. If prices are above C&F, can they be expected to remain there, and if so, why aren't commercial traders already capturing these margins? The CS starts out with a number of disadvantages relative to commercial players. Food aid is shipped under more risk averse freight terms resulting in higher costs. Food aid shipments often have delivery schedules that are less well defined than commercial shipments. Food aid purchases in the U.S. are done by the CCC, which does not have some of the origination and blending advantages of the commercial players. For these reasons, if a food aid sale is to meet the cost recovery benchmark, it must have other unique advantages. For example, the food aid might be: exempt from commercial duties and taxes; paid for in local currency, thus preserving precious foreign exchange reserves; destined for markets in high risk areas; permitted to circumvent formal channels. In summary, the CS's monetization request should be able to explain the source and magnitude of its commercial advantages.

b. If the monetization is intended to improve food security, the CS understands why the market is failing vulnerable households now. The CS should be able to explain the reasons that prices or trade flows do not reflect total costs and how a monetization will improve the functioning of the market. This explanation should include reference to market structure at stages where the price margins appear out of line and, wherever possible, some price history to indicate whether or not the current situation is an anomaly.

12. Ongoing Monitoring - If the market analysis indicates that a monetization will likely make sense, the CS should establish a process of regularly monitoring price and other relevant market information. In addition, the CS's efforts to understand specific components of the market structure should be ongoing. Impact analysis for a monetization will depend upon continued monitoring of the market. Interviews with traders will be an important part of the follow-up as traders will often be able to identify implications for the market that external monitoring of the data will not reveal.

13. Clarify Commodity Specifications - Prior to the call forward, it will be important for the CS to confirm the specifications of commodities to be monetized. Remember that the buyers of a monetized commodity must choose the product over other alternatives available in the market. Understand how the commodity will be used. For example, if the commodity to be monetized is vegetable oil, will U.S. soybean oil be acceptable in terms of taste and flash points; if it is wheat, will strong flour be preferred to weak flour or vice versa; if it is beans, will U.S. style pinto beans trade at a premium or discount to the prices observed in local markets? It is advisable for the CS to have a sample of U.S. product available since verbal descriptions tend to be inadequate. For refined products, it may be advisable to have a sample of domestic product analyzed to determine specifications.

14. Preparing for a Negotiation - For markets where the level of competition is inadequate to guarantee a fair tender, negotiation will be the vehicle for setting the sales price. In this case, a firm sales agreement must be drawn up to accompany the call forward request. In general, selling in this manner will not be advisable for monetizations designed to improve food security but may be necessary in certain settings where the only objective is to generate as much foreign currency as possible. When conducting negotiated sales, the CS should be aware of the least- cost alternate supply of a similar product to the same market location to be delivered in the proposed time frame. The CS should impress upon the buyer the advantages to be gained from buying the monetized commodity, such as:

a. paying for the commodity in local currency;

b. purchasing the commodity without assuming risks associated with dispatch freight terms that are often passed on to commercial buyers;

c. any advantages that would accrue to the buyer as a result of payment terms that would be different from full commercial transactions.

15. Demonstrating Market Competition - For markets where the level of competition is adequate to conduct a tender, evidence that the market is in fact competitive should be included in the monetization request in the CS's proposal.

D. Summary

Market analysis is the key to successful monetization. On the one hand, good market information allows the CS to prevent individual traders from capturing the entire benefit of the transaction. Perhaps more importantly, market information protects the market from ill-informed actions of inexperienced traders who are not subject to the same restrictions as commercial players. USAID is moving toward requiring more information in this area. However, it is hoped that the CS community will collect this information to improve its programming rather than simply to satisfy USAID requirements.

Appendix C - Monetization Profile

COUNTRY ____

FISCAL YR/CALL FORWARD # ______________________________________

COMMODITY TYPE & TONNAGE _____________________________________

SALES METHOD USED ____
(tender bid, lottery, negotiated sale)

PRICING SYSTEM USED ____
(stop-out; fixed price; average of bids; pay-bid)

EXCHANGE RATE USED ____

METHOD OF PAYMENT ____
(letter of credit; bank guarantee; cash; bank guarantee/cash)

NUMBER OF BIDS RECEIVED _______________________________________

LOWEST BID; HIGHEST BID ____

COOPERATING SPONSOR (CS) TARGET PRICE __________________________

CS MINIMUM PRICE; MAXIMUM PRICE _______________________________

NUMBER OF BUYERS ____

FAS QUOTATION ______________ FOREIGN FLAG ESTIMATE OR RATE _______

OTHER CHARGES AS APPLICABLE _________________
(See Implementation Section 1.C. Cost Recovery Benchmark)

SALES PRICE(S) ____
(in U.S. dollars and, if pay-bid used, final sales price by buyer)